

104TH CONGRESS  
1ST SESSION

# S. 1053

To amend the Internal Revenue Code of 1986 to promote capital formation  
for the development of new businesses.

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## IN THE SENATE OF THE UNITED STATES

JULY 20 (legislative day, JULY 10), 1995

Mr. LIEBERMAN (for himself and Mr. D'AMATO) introduced the following bill;  
which was read twice and referred to the Committee on Finance

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## A BILL

To amend the Internal Revenue Code of 1986 to promote  
capital formation for the development of new businesses.

1       *Be it enacted by the Senate and House of Representa-*  
2       *tives of the United States of America in Congress assembled,*

3       **SECTION 1. SHORT TITLE.**

4       This Act may be cited as the “Entrepreneurial New  
5       and Small Business Capital Formation Act of 1995”.

6       **SEC. 2. ROLLOVER OF CAPITAL GAINS ON CERTAIN SMALL**  
7       **BUSINESS INVESTMENTS.**

8       (a) IN GENERAL.—Part III of subchapter O of chap-  
9       ter 1 of the Internal Revenue Code of 1986 (relating to

1 common nontaxable exchanges) is amended by adding at  
2 the end the following new section:

3 **“SEC. 1045. ROLLOVER OF GAIN ON SMALL BUSINESS IN-**  
4 **VESTMENTS.**

5 “(a) NONRECOGNITION OF GAIN.—In the case of the  
6 sale of any eligible small business investment with respect  
7 to which the taxpayer elects the application of this section,  
8 gain from such sale shall be recognized only to the extent  
9 that the amount realized on such sale exceeds—

10 “(1) the cost of any other eligible small busi-  
11 ness investment purchased by the taxpayer during  
12 the 6-month period beginning on the date of such  
13 sale, reduced by

14 “(2) any portion of such cost previously taken  
15 into account under this section.

16 This section shall not apply to any gain which is treated  
17 as ordinary income for purposes of this subtitle.

18 “(b) DEFINITIONS AND SPECIAL RULES.—For pur-  
19 poses of this section—

20 “(1) PURCHASE.—The term ‘purchase’ has the  
21 meaning given such term by section 1043(b)(4).

22 “(2) ELIGIBLE SMALL BUSINESS INVEST-  
23 MENT.—Except as otherwise provided in this sec-  
24 tion, the term ‘eligible small business investment’  
25 means any stock in a domestic corporation, and any

1 partnership interest in a domestic partnership,  
2 which is originally issued after December 31, 1994,  
3 if—

4 “(A) as of the date of issuance, such cor-  
5 poration or partnership is a qualified small  
6 business entity, and

7 “(B) such stock or partnership interest is  
8 acquired by the taxpayer at its original issue  
9 (directly or through an underwriter)—

10 “(i) in exchange for money or other  
11 property (not including stock), or

12 “(ii) as compensation for services  
13 (other than services performed as an un-  
14 derwriter of such stock or partnership in-  
15 terest).

16 A rule similar to the rule of section 1202(c)(3) shall  
17 apply for purposes of this section.

18 “(3) ACTIVE BUSINESS REQUIREMENT.—Stock  
19 in a corporation, and a partnership interest in a  
20 partnership, shall not be treated as eligible small  
21 business investment unless, during substantially all  
22 of the taxpayer’s holding period for such stock or  
23 partnership interest, such corporation or partnership  
24 meets the active business requirements of subsection  
25 (c). A rule similar to the rule of section

1 1202(c)(2)(B) shall apply for purposes of this sec-  
2 tion.

3 “(4) QUALIFIED SMALL BUSINESS ENTITY.—

4 “(A) IN GENERAL.—The term ‘qualified  
5 small business entity’ means any domestic cor-  
6 poration or partnership if—

7 “(i) for the taxable year of such entity  
8 in which the stock or partnership interest  
9 was issued and each prior taxable year,  
10 such entity (and any predecessor thereof)  
11 had gross receipts of less than  
12 \$20,000,000,

13 “(ii) at all times before such issuance,  
14 such entity (and any predecessor thereof)  
15 had aggregate gross assets (as defined in  
16 section 1202(d)(2)) of less than  
17 \$25,000,000, and

18 “(iii) at all times before such issu-  
19 ance, the excess of the fair market value of  
20 the assets of such entity (and any prede-  
21 cessor thereof) over the liabilities of such  
22 entity was less than \$10,000,000.

23 “(B) AGGREGATION RULES.—All persons  
24 treated as a single employer under subsection

1 (a) or (b) of section 52 shall be treated as one  
2 person for purposes of subparagraph (A).

3 “(C) SPECIAL RULES FOR DETERMINING  
4 GROSS RECEIPTS.—The rules of subparagraphs  
5 (B) and (C) of section 448(c)(3) shall apply for  
6 purposes of subparagraph (A)(i).

7 “(c) ACTIVE BUSINESS REQUIREMENT.—

8 “(1) IN GENERAL.—For purposes of subsection  
9 (b)(3), the requirements of this subsection are met  
10 by a qualified small business entity for any period  
11 if—

12 “(A) the entity is engaged in the active  
13 conduct of a trade or business, and

14 “(B) at least 80 percent (by value) of the  
15 assets of such entity are used in the active con-  
16 duct of a trade or business.

17 “(2) SPECIAL RULE FOR CERTAIN ACTIVI-  
18 TIES.—For purposes of paragraph (1), if, in connec-  
19 tion with any future trade or business, an entity is  
20 engaged in—

21 “(A) startup activities described in section  
22 195(c)(1)(A),

23 “(B) activities resulting in the payment or  
24 incurring of expenditures which may be treated

1 as research and experimental expenditures  
2 under section 174, or

3 “(C) activities with respect to in-house re-  
4 search expenses described in section 41(b)(4),  
5 such entity shall be treated with respect to such  
6 activities as engaged in (and assets used in  
7 such activities shall be treated as used in) the  
8 active conduct of a trade or business. Any de-  
9 termination under this paragraph shall be made  
10 without regard to whether the entity has any  
11 gross income from such activities at the time  
12 of the determination.

13 “(3) CERTAIN RULES TO APPLY.—Rules similar  
14 to the rules of paragraphs (5), (6), (7), and (8) of  
15 section 1202(e) shall apply for purposes of this sub-  
16 section.

17 “(d) CERTAIN OTHER RULES TO APPLY.—Rules  
18 similar to the rules of subsections (f), (g), (h), and (j)  
19 of section 1202 (without regard to any 5-year holding pe-  
20 riod requirement) shall apply for purposes of this section.

21 “(e) BASIS ADJUSTMENTS.—If gain from any sale is  
22 not recognized by reason of subsection (a), such gain shall  
23 be applied to reduce (in the order acquired) the basis for  
24 determining gain or loss of any eligible small business in-

1 vestment which is purchased by the taxpayer during the  
2 6-month period described in subsection (a).

3 “(f) STATUTE OF LIMITATIONS.—If any gain is real-  
4 ized by the taxpayer on the sale or exchange of any eligible  
5 small business investment and there is in effect an election  
6 under subsection (a) with respect to such gain, then—

7 “(1) the statutory period for the assessment of  
8 any deficiency with respect to such gain shall not ex-  
9 pire before the expiration of 3 years from the date  
10 the Secretary is notified by the taxpayer (in such  
11 manner as the Secretary may by regulations pre-  
12 scribe) of—

13 “(A) the taxpayer’s cost of purchasing  
14 other eligible small business investment which  
15 the taxpayer claims results in nonrecognition of  
16 any part of such gain,

17 “(B) the taxpayer’s intention not to pur-  
18 chase other eligible small business investment  
19 within the 6-month period described in sub-  
20 section (a), or

21 “(C) a failure to make such purchase with-  
22 in such 6-month period, and

23 “(2) such deficiency may be assessed before the  
24 expiration of such 3-year period notwithstanding the

1 provisions of any other law or rule of law which  
 2 would otherwise prevent such assessment.

3 “(g) REGULATIONS.—The Secretary shall prescribe  
 4 such regulations as may be appropriate to carry out the  
 5 purposes of this section, including regulations to prevent  
 6 the avoidance of the purposes of this section through  
 7 splitups, shell corporations, partnerships, or otherwise.”

8 (b) CONFORMING AMENDMENT.—Paragraph (23) of  
 9 section 1016(a) of such Code is amended—

10 (1) by striking “or 1044” and inserting “,  
 11 1044, or 1045”, and

12 (2) by striking “or 1044(d)” and inserting “,  
 13 1044(d), or 1045(e)”.

14 (c) CLERICAL AMENDMENT.—The table of sections  
 15 for part III of subchapter O of chapter 1 of such Code  
 16 is amended by adding at the end the following new item:

“Sec. 1045. Rollover of gain on small business investments.”

17 (d) EFFECTIVE DATE.—The amendments made by  
 18 this section shall apply to taxable years ending after De-  
 19 cember 31, 1994.

20 **SEC. 3. LOSSES ON ELIGIBLE SMALL BUSINESS INVEST-**  
 21 **MENTS.**

22 (a) IN GENERAL.—Part IV of subchapter P of chap-  
 23 ter 1 of the Internal Revenue Code of 1986 (relating to  
 24 special rules for determining gains and losses) is amended  
 25 by inserting after section 1244 the following new section:



1   **“SEC. 1244A. LOSSES ON ELIGIBLE SMALL BUSINESS IN-**  
2                           **VESTMENTS.**

3        “If—

4               “(1) a loss is on any eligible small business in-  
5       vestment (as defined in section 1045(b)), and

6               “(2) such loss would (but for this section) be a  
7       loss from the sale or exchange of a capital asset,  
8       then such loss shall be treated as an ordinary loss. For  
9       purposes of section 172 (relating to the net operating loss  
10      deduction), any amount of loss treated by reason of this  
11      section as an ordinary loss shall be treated as attributable  
12      to a trade or business of the taxpayer.”

13       (b) CLERICAL AMENDMENT.—The table of sections  
14      for such part IV is amended by inserting after the item  
15      relating to section 1244 the following new item:

              “Sec. 1244A. Losses on eligible small business investments.”

16       (c) EFFECTIVE DATE.—The amendments made by  
17      this section shall apply to taxable years ending after De-  
18      cember 31, 1994.

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